

SURREBUTTAL TESTIMONY
AND EXHIBITS
OF
STEVEN W. HAMM
ON BEHALF OF
THE SOUTH CAROLINA OFFICE OF REGULATORY STAFF
DOCKET NO. 2018-318-E
IN RE: APPLICATION OF DUKE ENERGY PROGRESS, LLC
FOR ADJUSTMENTS IN ELECTRIC RATE SCHEDULES AND TARIFFS AND
REQUEST FOR AN ACCOUNTING ORDER

Q. PLEASE STATE YOUR NAME, BUSINESS ADDRESS AND OCCUPATION.

A. My name is Steven W. Hamm. My business address is 1401 Main Street, Suite 900, Columbia, South Carolina 29201. I am employed by the State of South Carolina as Special Counsel and Senior Advisor, in the Legal Department of the South Carolina Office of Regulatory Staff (“ORS”).

Q. HAVE YOU PREVIOUSLY APPEARED BEFORE THE PUBLIC SERVICE COMMISSION OF SOUTH CAROLINA?

A. Yes. I appeared as Legal Counsel in my first contested case hearing before the Public Service Commission of South Carolina (“Commission” or “PSC”) over 40 years ago, in the summer of 1978. At that point, I served as State Deputy Consumer Advocate and head of the newly created Division of Consumer Advocacy at the South Carolina Department of Consumer Affairs. I was named Administrator and State Consumer Advocate for the Department in 1981 by the Commission on Consumer Affairs. I served

1 at the Department of Consumer Affairs for almost 18 years and left the Department to enter
2 the private practice of law in 1994. I represented many regulated entities before the
3 Commission during my 24 years in private practice. I have appeared before the
4 Commission in various types of regulatory proceedings. I left private practice and joined
5 ORS in September 2018.

6 **Q. WHAT IS THE PURPOSE OF YOUR SURREBUTTAL TESTIMONY?**

7 **A.** The purpose of my surrebuttal testimony is to address the regulatory policy issues
8 related to certain legal expenses sought by Duke Energy Progress, LLC (“DEP” or
9 “Company”) which are addressed in the rebuttal testimony of DEP witness Laura Bateman,
10 Dr. Julius Wright and Barbara Coppola. I will discuss why ORS recommends the
11 Commission disallow cost recovery from customers for those identified legal expenses.

12 **Q. HAS REGULATORY PUBLIC POLICY CHANGED AND EVOLVED DURING**
13 **YOUR CAREER OF APPEARING BEFORE THE COMMISSION?**

14 **A.** Yes. I have been directly involved in working to shape and revise the regulatory
15 public policy standards that serve to guide the Commission in evaluating rate making
16 positions advanced by regulated companies. Rulings by the South Carolina Supreme Court
17 in response to appeals of Commission orders have been a significant factor in how the
18 Commission decides contested issues.

19 **Q. WHAT CHANGES HAVE YOU OBSERVED DURING THE PAST 40 YEARS OF**
20 **APPEARING BEFORE THE COMMISSION?**

21 **A.** The Commission has modified policy positions in response to efforts by regulated
22 companies to claim that a utility should be able to recover all costs of operations from
23 ratepayers, regardless of who benefitted from those expenses.

Q. CAN YOU PROVIDE THE COMMISSION WITH AN EXAMPLE?

A. Yes. In a recent Carolina Water Service, Inc. (“CWS”) rate case, the Commission addressed whether the contested proposed legal expenses should be paid by customers. Based upon the record testimony and evidence, the Commission ruled that certain CWS litigation expenses should be assigned to stockholders and not customers.¹

Q. HOW WOULD YOU DESCRIBE THE CURRENT LEGAL EXPENSE REGULATORY POLICY ADOPTED BY THE COMMISSION?

A. I believe the current Commission approach to examine proposed legal expense recovery is focused on a determination of whether the underlying legal expenses in question should be paid by customers. The Commission regulatory policy includes an examination of the legal expenses to determine if the Company’s legal costs and expenses were the result of prior management decisions. The Commission will generally not include legal costs and expenses in rates paid by customers in legal disputes in which the Company was found at fault and was unable to reverse that finding of fault.

Q. WHY SHOULD MANAGEMENT DECISIONS AND ACTIONS AFFECT WHETHER OR NOT PROPOSED LEGAL EXPENSES SHOULD BE RECOVERED BY CUSTOMERS?

A. The rates and charges for public utility service in South Carolina are required by law to meet the regulatory standard of being both fair and reasonable to customers and provide a reasonable rate of return to Company investors. Those rates allow the Company to operate in a lawful manner. Company management is required to take all necessary steps to comply with applicable legal and regulatory requirements. Final Commission orders

¹ Docket No. 2017-292-WS – Order 2018-802

1 must reflect a proper application of Company and customers' interests which require a full
2 examination of why those expenses were incurred in the first place. The South Carolina
3 Supreme Court has confirmed and ruled that the Commission has the regulatory authority
4 to reject portions of expenses previously incurred by a regulatory utility.²

5 **Q. HOW DOES DEP ATTEMPT TO SUPPORT PAYMENT OF COAL ASH**
6 **LITIGATION COSTS?**

7 **A.** DEP filed Direct and Rebuttal Testimony for Dr. Julius Wright that briefly
8 addressed coal ash legal costs related to insurance recovery litigation and the legal defense
9 costs of North Carolina enforcement action.

10 **Q. DOES DR. WRIGHT PROVIDE ANY SPECIFIC LEGAL DATA, COURT**
11 **DECISIONS, OR OTHER INFORMATION TO JUSTIFY COAL ASH RELATED**
12 **LEGAL EXPENDITURES BY DEP?**

13 **A.** No.

14 **Q. PLEASE EXPLAIN.**

15 **A.** Dr. Wright makes no detailed presentation to justify that DEP wants its customers
16 to pay all legal costs and expenses. Dr. Wright makes the broad assertion that "legal fees
17 should be recoverable because they represent a legitimate, reasonable and prudent business
18 expenditure." Dr. Wright does not explain why customers should pay the legal expenses
19 including litigation expenses associated with a breach of contract case that resulted in an
20 adverse court decision and later settlement. The legal expense information supplied by DEP
21 is not case specific.

² *Utilities Services of SC v. SC Office of Regulatory Staff*, 392 S.C. 96, 708 S.E.2d 755 (2011).

Q. WHAT BASIS DOES DEP WITNESS BATEMAN OFFER TO THE COMMISSION?

A. Witness Bateman attempted to justify the vague and limited responses provided to ORS during discovery by defending the legal e-billing system used by the Company. The information contained in the Microsoft Excel print out provided no fundamental underlying data or information that could be used by ORS to confirm exactly which case, matter or issue was being billed to DEP. ORS advised that information was not sufficient to support the legal expenses in question. The Company provided no further detailed information. The Company is responsible for maintaining information in a manner that allows full regulatory examination.

Q. DOES ORS'S PROPOSED DISALLOWANCE PREVENT DEP FROM DEFENDING ITSELF FROM LAWSUITS?

A. No.

Q. PLEASE EXPLAIN.

A. DEP has provided no substantive information for any coal ash litigation expenses to justify customers being responsible for legal fees and costs. Every proposed legal expense is always subject to a disallowance by the Commission based on a variety of considerations. Shareholders should pay the costs for litigation defending the Company where the Company did not prevail on claims of violations of state and federal law and regulations.

Q. HAS THE COMMISSION DISALLOWED LEGAL EXPENSES?

A. Yes.

Q. PLEASE EXPLAIN.

1 **A.** The Commission recently disallowed certain legal expenses requested by CWS in
2 a Reconsideration Order issued on January 25, 2019. The Commission declined to force
3 customers to pay for the Company's legal expenses related to its failure to successfully
4 overturn a federal court decision finding the Company in violation of the Clean Water Act.³

5 **Q. HAVE YOU EXAMINED THE LITIGATION COSTS AND EXPENSES SOUGHT**
6 **BY DEP IN THIS DOCKET?**

7 **A.** Yes.

8 **Q. SHOULD THE COMMISSION APPROVE ALL DEP LEGAL EXPENSES**
9 **SOUGHT IN THIS PROCEEDING BASED ON THE VERY SUMMARY**
10 **INFORMATION PROVIDED TO ORS DURING DISCOVERY?**

11 **A.** No.

12 **Q. PLEASE EXPLAIN YOUR RESPONSE TO THE COMMISSION.**

13 **A.** As an initial policy approach, ORS recommends that the Commission first
14 determine if the Company's proposed legal expense should be considered as a ratemaking
15 operating expense to be included in rates authorized by the Commission. "When litigation
16 involves claims asserting failure of the utility to adhere to state or federal law, we must
17 look carefully at the matter to determine whether expenses associated with defending the
18 action should be included in rates paid by customers." Docket No. 2017-292-WS, Order
19 No. 2018-802 p.16

20 **Q. ARE YOU SUGGESTING THAT A REGULATORY UTILITY MUST MEET A**
21 **PERFECTION STANDARD IN ORDER TO OBTAIN COST RECOVERY FROM**
22 **THE COMMISSION?**

³ Docket No. 2017-292-WS – Order 2018-802

1 **A.** No. The Commission has many years of experience examining complex cases from
2 regulating a wide range of regulated entities. What has changed over my 40 years of
3 experience before the Commission is the Commission now demands greater accountability
4 and greater underlying data and information before it approves Company requests for rate
5 adjustments.

6 **Q. PLEASE EXPLAIN THE LITIGATION EXPENSES AT ISSUE IN THIS RATE**
7 **PROCEEDING.**

8 **A.** DEP seeks ratepayer recovery of certain coal ash litigation expenses. Most notable
9 is the extremely summary explanation provided by DEP to ORS discovery inquiries.

10 DEP provided the very same limited written justification for several legal invoices
11 for coal ash litigation expenses. The description of services for the legal invoice, as
12 provided by DEP in its response to ORS states “legal fees and expenses related to potential
13 insurance recovery for coal ash.” Exhibits SWH-1 through SWH-4. The Company made
14 no reference to existing litigation cases and disputes or court orders that were adverse to
15 the Company. The Commission has no way, based upon Company responses, to know if
16 some or all of the litigation expenses were defending claims that the Company violated
17 state or federal law. The rates approved by the Commission require the Company to comply
18 with all laws that apply to its operations.

19 **Q. ARE THERE ANY DEP SUMMARIES FOR OTHER COAL ASH LEGAL**
20 **EXPENSES?**

21 **A.** Yes. DEP provided the following brief justification regarding multiple other listed
22 coal ash legal expenses. The description for services performed stated “Defense of coal
23 ash state enforcement litigation for DEP, LLC Sites based on alternative fee arrangement.”

DEP did not address why ratepayers should pay those costs since the litigation was based on allegations of unlawful conduct by the Company.

Q. PLEASE EXPLAIN WHY ORS RECOMMENDS THE COMMISSION EXCLUDE LEGAL COST RECOVERY OF COAL ASH LEGAL INVOICES.

A. DEP has not provided the Commission or ORS with any clear and detailed information supporting its claim for recovery of hundreds of thousand dollars of coal ash litigation expenses. The brief DEP explanations merely advise the Commission that DEP is defending unnamed Company actions related to coal ash cases filed against DEP. The Commission only knows that DEP believes there may be “*potential* insurance recovery for coal ash” (emphasis added). DEP has not demonstrated that any of the coal ash litigation expenses merit inclusion in the rates that may be established by the Commission in this DEP proceeding.

Q. WHAT IF A LEGAL FORUM HAVING JURISDICTION OVER DEP RULES THAT THE MASSIVE DEP COAL ASH DISCHARGE IN NORTH CAROLINA WAS THE RESULT OF DEP MANAGEMENT FAILURE?

A. DEP has the legal obligation to file any existing orders or decisions relating to coal ash matters with the Commission. Sound regulatory policy should require the review of specific positions by DEP and in related litigation proceedings before the Commission has any basis to make final regulatory decisions on what coal ash related litigation costs or expenses, if any, should be included in DEP rates in South Carolina.

Q. DOES DEP SEEK RECOVERY OF ANY OTHER LITIGATION COSTS AND EXPENSES IN THIS DOCKET?

1 **A.** Yes. DEP seeks recovery for costs and expenses arising out of DEP's breach of a
2 2012 contract with CertainTEED Gypsum, Inc. This litigation is also discussed in the
3 direct and surrebuttal testimonies of ORS witness Morgan. We know from a confidential
4 settlement agreement that the Company [REDACTED]
5 [REDACTED]. We do not know if any of those costs are included
6 in this rate proceeding.

7 **Q. WHY DOES DEP ASSERT THAT IT IS ENTITLED TO RECOVERY OF THESE**
8 **LITIGATION COSTS AND EXPENSES?**

9 **A.** Company witness Coppola asserts that the Company did not breach its contract and
10 that any legal fees the Company incurs to defend itself in lawsuits are proper for recovery
11 from customers. (*See* Coppola Rebuttal p. 5 ll. 8–16.) Witness Coppola provided no
12 evidential basis for her claims.

13 **Q. ARE THE REASONS FOR RECOVERY PROFFERED BY COMPANY WITNESS**
14 **COPPOLA COMPELLING?**

15 **A.** No. The overwhelming evidence shows that DEP breached the CertainTEED
16 contract. There is a valid final judgment finding DEP was in breach that was not overturned
17 and later settled [REDACTED] (and at this point,
18 will never be) overturned (*see* Exhibit WJM-2 at 77–82; Confidential Exhibit WJM-3);
19 DEP paid approximately \$1,084,000 for its breach. DEP also agreed to [REDACTED]
20 [REDACTED] as part of its settlement with CertainTEED (*see*

Confidential Exhibit WJM-3).⁴ Customers should not be held responsible for the Company's actions that led to a breach of contract that the Company and its management negotiated. And customers should not be held responsible for the Company's decision to pursue intensive litigation that ended in the Company [REDACTED]

(See Confidential Exhibit WJM-3). It is impossible to know, based on information supplied by DEP, if any of those legal expenses are present in this rate proceeding,

Q. DOES THE ORS POSITION DISCOURAGE THE COMPANY FROM ENTERING INTO CONTRACTS OR FROM PURSUING MERITORIOUS LITIGATION IF NECESSARY?

A. No. ORS's position helps to align the costs and benefits of entering into agreements such as the CertainTEED contract. Disallowing expenses where the Company breaches its agreements serves to encourage careful negotiation and assessment of the potential and the pitfalls of a particular agreement. It also helps to ensure that the Company carefully manage its operation and consider the costs that pursuing litigation could potentially have for its customers. Sound policy requires that the Company should not be able to insulate its shareholders by externalizing costs to customers.

Q. DOES ORS RECOMMEND THE COMMISSION APPROVE RATES WHICH INCLUDE THE ADVERSE COST IMPACTS RESULTING FROM POOR DEP MANAGEMENT DECISIONS?

⁴ Black's Law Dictionary defines [REDACTED]. (Available at: <https://thelawdictionary.org/> [REDACTED]) (emphasis added).

1 **A.** ORS believes the only sound regulatory policy answer is no. ORS recommends the
2 Commission review and consider all relevant management and legal factors before it
3 approves any specific expenses. The evolving regulatory environment and concerns from
4 the General Assembly clearly point to the conclusion that Company management will not
5 be rewarded for failure to comply with federal and state laws.

6 **Q. DOES THIS CONCLUDE YOUR SURREBUTTAL TESTIMONY?**

7 **A.** Yes, it does.